

The equity of government support for retirement income

28th Colloquium on Pensions and Retirement Research

9 December 2020

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Agenda

- Starting point – forms of government support
- Consultation paper for the RIR
- Final report from the RIR
- Alternative assumption
- Comparisons of options
- Some conclusions

Forms of government support to providing retirement income

- **Direct expenditure to retirees**

- Age Pension received by 65% of those over AP eligibility age

- 42% of those aged 66 rising to 80% of those aged over 80

- Veterans pension received by a further 3%

- Other forms of income support (eg. DSP, Carers) – a further 3%

- **Tax concessions for superannuation**

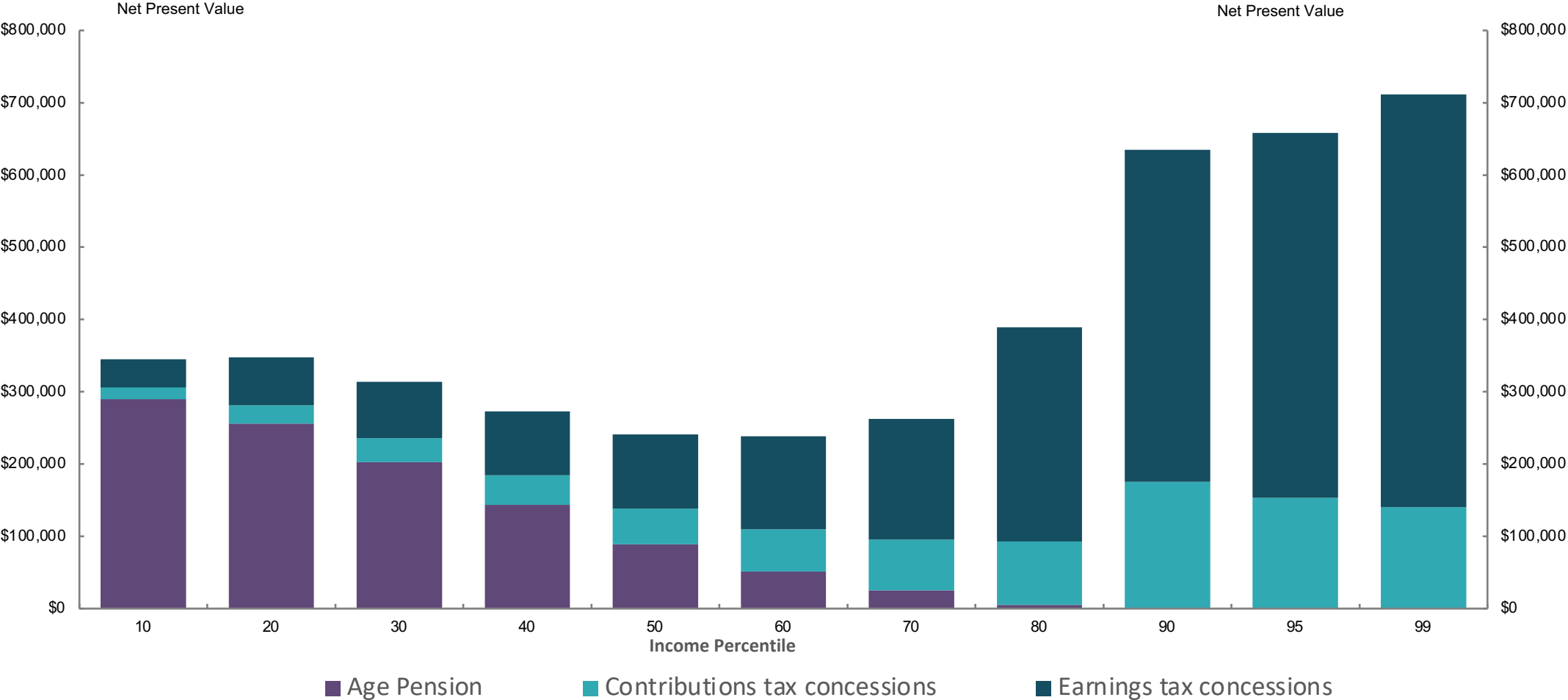
- Contributions – Div 293; LISTO

- Investment earnings before pension phase

- Investment earnings during pension phase

Consultation Paper for the RIR – Figure 4

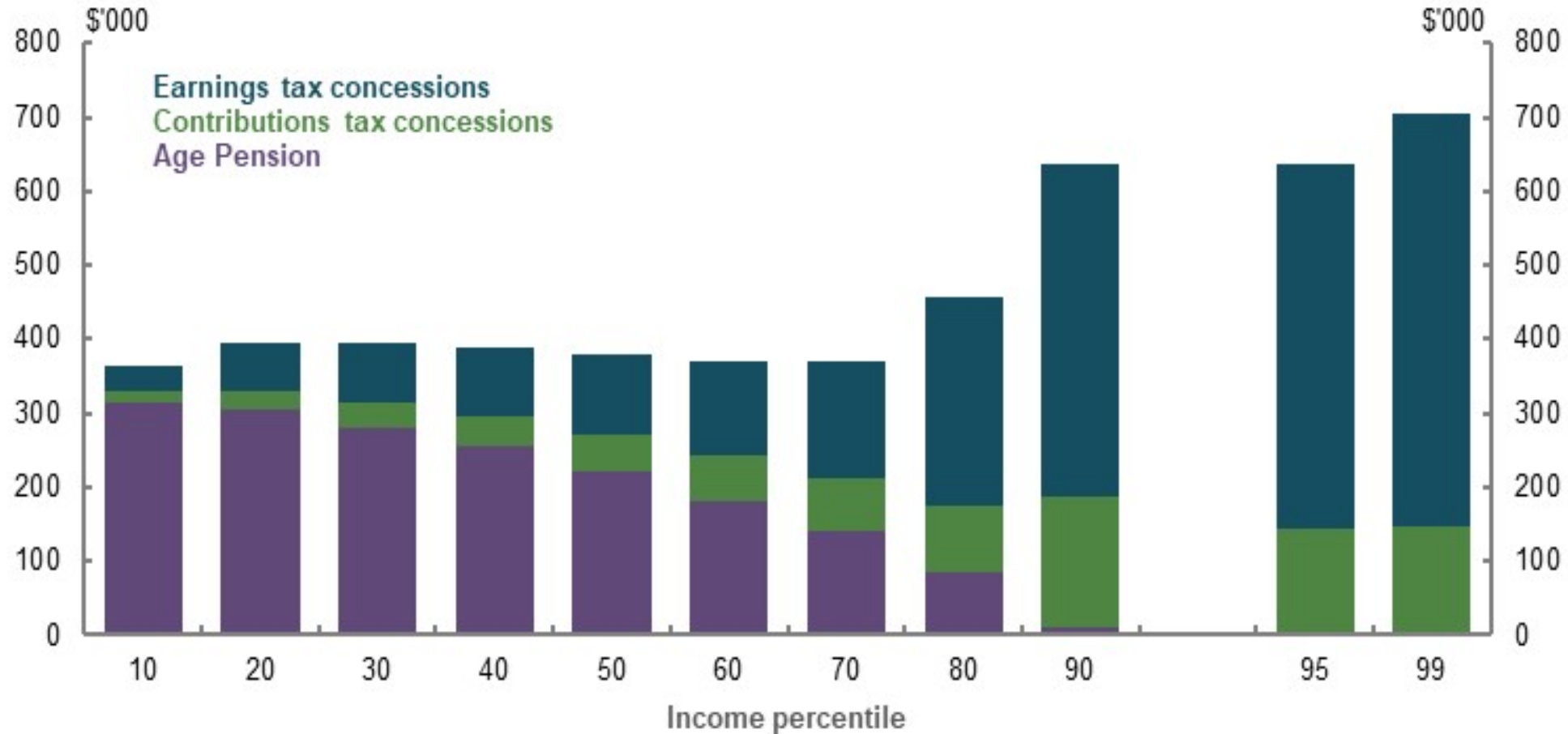
Lifetime government support provided through the retirement income system



Some of the assumptions used as per their footnote

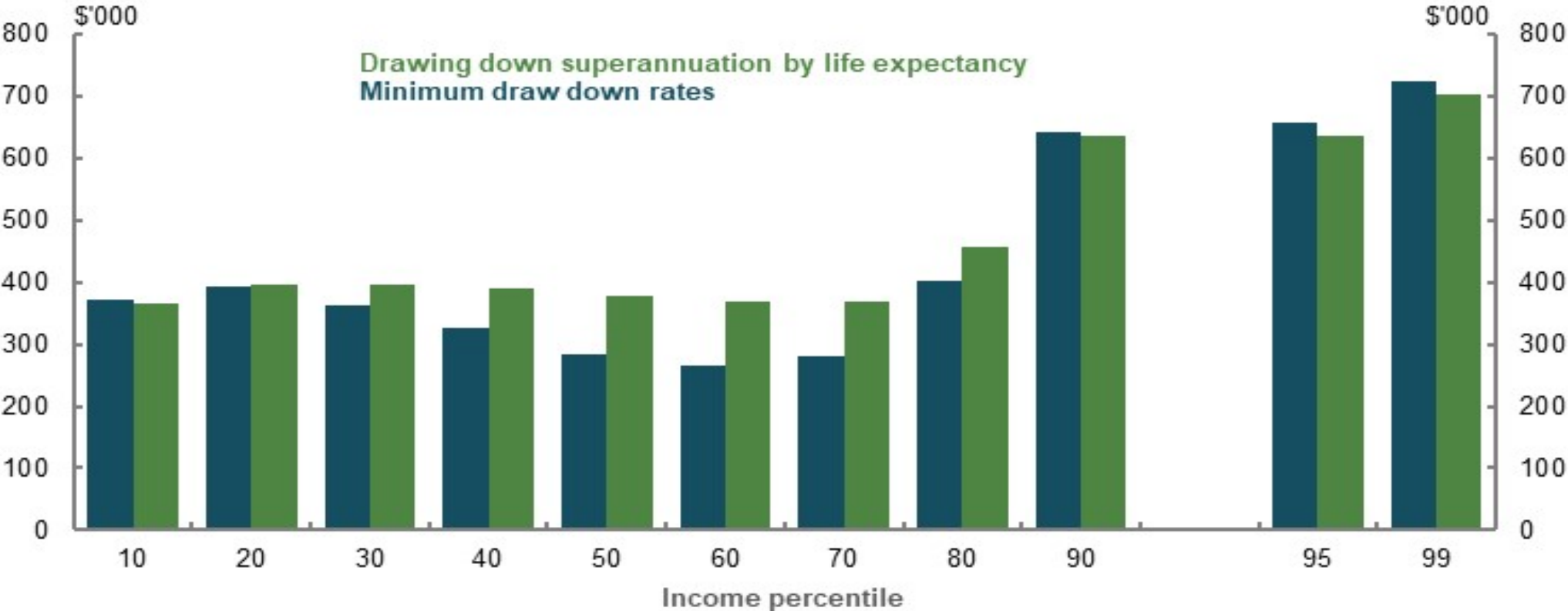
- Individuals commence work in 2018-19 at age 27 and work until age 67, with a predicted life expectancy of 92.
- Accumulated superannuation benefits are invested in an account based pension and individuals are assumed to draw down their assets at current age based **minimum drawdown rates**.
- The level of tax assistance and Age Pension entitlements are discounted by nominal gross domestic product (**around 5 per cent per annum**) to give a net present value in 2018-19 dollars.
- Annual incomes are calculated for each percentile based on the distribution of earners at each single year of age. Assumes no non-concessional contribution

The RIR Report shows something different - Chart 3A-11



Values are in 2019-20 dollars, deflated using the review's GDP deflator and uses review assumptions. Middle-income earners receive less support when superannuation is drawn down in line with the minimum legislated rates.

Projected lifetime Government support provided through the retirement income system, by drawdown strategy: Chart 3A-17



“The distribution of lifetime Government support does not significantly change under the minimum drawdown rates, compared with drawing down superannuation to exhaust at life expectancy.” p256

The use of the GDP deflator

- **From the Government's perspective**

- “The Government can fund the cost of Age Pension expenditure and superannuation tax concessions through borrowing or future tax receipts.” p254
- “Economic theory suggests that in the long run government bond rates will be marginally higher than nominal GDP growth” p254

- **From the individual's perspective**

- How much retirement income is the Government “giving” me?
- Is it fair?
- RIR report use mixed deflator - wages (4%) & CPI (2.5%) – in respect of future income

Replicating the Consultation Paper numbers Based on minimum drawdown rates



Reducing the deflator from GDP to 3.5% pa

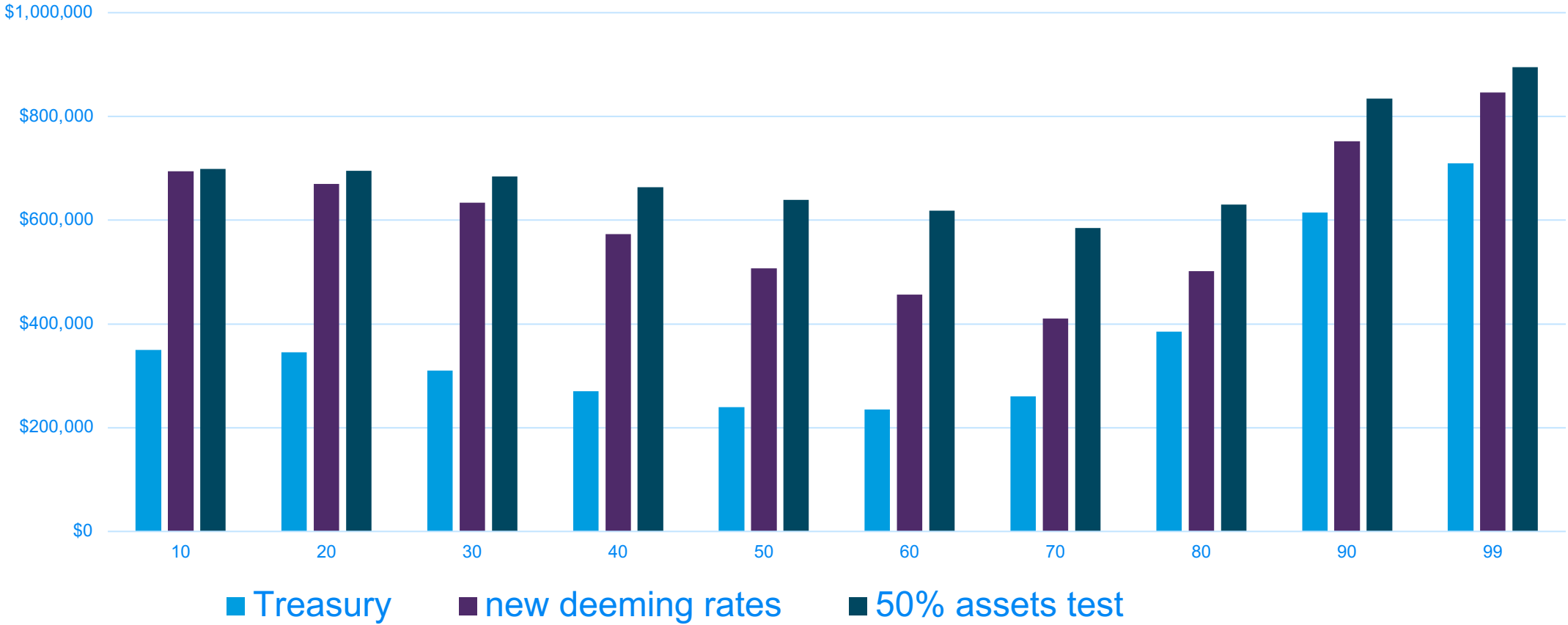
Naturally present values increase



Let's reduce the investment returns by 1%



The impact of 2020 deeming rates and halving the assets test taper



A review of the options

Modelling scenario	Coefficient of variation
Treasury numbers	0.437
Mercer base at 5% deflator	0.427
Mercer base at 3.5% deflator	0.314
Reduction in returns by 1% pa	0.173
Reduction in nominal rates by 0.5% pa	0.230
New deeming rates	0.230
Halving the assets test taper	0.141

CV = standard deviation/mean

Some comments about measuring tax concessions

- From the RIR report
 - “Equity has no universal measure” p234
 - “The cost of superannuation tax concessions — although difficult to measure — is projected to increase as a percentage of GDP as the superannuation system matures.” p375
 - “The cost of tax concessions is not observed but estimated by comparing actual revenue received with what might have been collected in the absence of concessions. Constructing this counterfactual is not straightforward.” p379
 - “The (projected) cost of tax concessions is estimated independently each year (i.e. there is no dynamic impact of the removal of concessions over time).” p376

The deflator

- A GDP deflator may be appropriate for Government finances but ...
- It is not appropriate to measure equity (or fairness) between individuals
 - We need a rate that is relevant to individuals
 - The answers are very different because we are looking at very long periods
- A reduced deflator
 - Increases the value of future Age Pension payments more than tax concessions
 - Highlights the situation of average income earners

welcome to

brighter

